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Attorney for Specially Appearing Claimant COVER DRIVE INC.

**UNITED STATES DISTRICT COURT  
CENTRAL DISTRICT OF CALIFORNIA**

CAPITAL BANK PLC. (a subsidiary of )  
Bank of Scotland) )

Plaintiff, )

vs. )

M/Y BIRGITTA, Official No.: 910659, )  
and her engines, tackle and apparel etc., )  
in rem; and JUANITA GROUP )  
LIMITED, in personam, )

Defendants. )

Case No. 2:08-cv-05893-PSG (SSx)  
IN ADMIRALTY

MEMORANDUM OF CONTENTIONS OF  
FACT AND LAW  
[L.R. 16-4]

Pretrial Conference: June 28, 2010  
Court Trial: July 13, 2010

Assigned to: The Hon. Philip S. Gutierrez  
Courtroom: 880, Roybal Building  
Complaint Filed: September 9, 2008

Pursuant to Local Rule 16-4, Specially Appearing Claimant and Defendant  
COVER DRIVE INC. respectfully submits this Memorandum of Contentions of Fact and Law.

**CLAIMS AND DEFENSES**

**I. Claims of Plaintiff Capital Bank PLC**

Claim 1: Breach of Contract - *In Personam*

Claim 2: Breach of Contract - *In Rem*

**A. Elements Required to Establish Plaintiff's Claims**

1. In rem jurisdiction over defendant vessel BIRGITTA (the existence of a foreign preferred ship mortgage as required by the Maritime Commercial Instruments and Liens Vessel Identification System Act of 1988 (46 USC §§31301 et seq.), formerly

1 known as the Ship Mortgage Act (hereafter “SMA”).

2 2. In personam jurisdiction over Specially Appearing Defendant and Claimant  
3 JUANITA.

4 3. The existence of an enforceable contract under the laws of England.

5 4. An actionable breach of that contract.

6 5. Damages proximately caused by that breach.

7 **B. Key Evidence in Opposition to Plaintiff’s Claims**

8 1. The deposition testimony of JUANITA’s former shareholder and director Carl  
9 Freer, expert testimony and supporting documents will establish that the CAPITAL  
10 BANK mortgage had to be registered at both ROSS and Companies House in the UK  
11 because at all relevant times JUANITA had an established place of business in the UK,  
12 the BIRGITTA was in the UK, JUANITA was owned and operated by UK residents,  
13 and engaged in significant commercial activity in the UK.

14 2. Plaintiff’s admission that it did not register its mortgage with Companies  
15 House in England. (Stipulated Fact 34 - Pacer Document 35.)

16 3. Documents and testimony establishing that COVER DRIVE registered its  
17 mortgage with both ROSS and with Companies House, including Joint Exhibit 290.

18 4. Documents and testimony establishing that JUANITA purchased the  
19 BIRGITTA from COVER DRIVE for conditional consideration, of which CAPITAL  
20 BANK knew or should have known prior to making the \$6 million loan to JUANITA,  
21 which consideration was rendered worthless through no fault of COVER DRIVE, as a  
22 consequence of which JUANITA granted a valid ship’s mortgage to COVER DRIVE,  
23 which has priority over the CAPITAL BANK mortgage.

24 5. If before trial, as currently anticipated, liquidation proceedings are initiated in  
25 England, Plaintiff’s mortgage may well be declared void, relegating Plaintiff to the  
26 status of a general unsecured creditor. Upon that occurrence, not only will Plaintiff not  
27 have a preferred ship mortgage under U.S. law, but also will have no mortgage under  
28 English law.

6. Testimony and documents will establish that before the original arrest of the BIRGITTA in May 2006: (a) there were no breaches of contract; (b) there were no payment or insurance defaults; (c) Plaintiff had either waived the UK waters restriction or consented to the BIRGITTA being in U.S. waters; and, (d) Plaintiff had no reasonable grounds to believe its security was in jeopardy.

7. Plaintiff has failed to mitigate its damages by: (a) arresting the BIRGITTA in May 2006 without factual or legal grounds to do so; and (b) refusing to accept a January-March 2007 good faith all cash offer by a third party to purchase the BIRGITTA for \$6.25 million. That amount would have paid Plaintiff all of its damages claims (including all arrest costs, attorneys' fees, accrued interest and the full amount outstanding under the loan). COVER DRIVE contends that this absolute failure to mitigate damages means that Plaintiff cannot establish the damages element of its claim.

## II. Claims of Claimant COVER DRIVE INC.

Claim 1: Specially Appearing Claimant and Defendant COVER DRIVE INC. filed a verified Statement of Claim asserting its ownership interest in the BIRGITTA based on having received a ship's mortgage for good and valuable consideration, and duly registered the mortgage with ROSS and with Companies House. CAPITAL BANK contests COVER DRIVE's claim; BIRGITTA does not.

### A. Elements of COVER DRIVE's Claim.

1. A valid ship's mortgage under the laws of the United Kingdom.
2. Valid registration of its mortgage with ROSS and Companies House.
3. Priority over CAPITAL BANK's mortgage.

## III. COVER DRIVE's Affirmative Defenses

First Affirmative Defense: Lack of Subject Matter Jurisdiction

Second Affirmative Defense: Failure to Mitigate Damages

Third Affirmative Defense: Existence of a Superior Security Interest

### A. Elements Required to Establish COVER DRIVE's First Affirmative Defense

1 First Affirmative Defense: Lack of Subject Matter Jurisdiction:

2 Neither the Exhibits to the First Amended Complaint nor any other  
 3 documents constitute a duly registered ship mortgage under  
 4 English Law in Plaintiff's favor, and therefore Plaintiff does not  
 5 have a foreign preferred ship mortgage under 46 U.S.C. § 31301 on  
 6 the Vessel and this Court has no subject matter jurisdiction over  
 7 this dispute.

8 1. The Court's subject matter jurisdiction stems directly and exclusively from  
 9 the provisions of the Maritime Commercial Instruments and Liens Vessel Identification  
 10 System Act of 1988 (46 USC Sec. 31301, et seq.), formerly known as the Ship  
 11 Mortgage Act (hereafter "SMA"). 46 USC Sec. 31301(6) (B).

12 2. In order to constitute a preferred mortgage under the SMA, a ship mortgage  
 13 on a foreign vessel must be registered in compliance with the laws of the applicable  
 14 foreign country. ("...a mortgage can only be deemed a 'referred mortgage' if it has  
 15 been registered in accordance with applicable foreign law." Court Order of  
 16 December 2, 2009, Doc. 117, pg. 4.)

17 3. The applicable foreign law in this case is English, and English Law requires  
 18 dual registration of company-owned vessels:

19 Dual registration requirement. There is no statutory exemption  
 20 under the company charges registration system in relation to a  
 21 registered or registrable ship mortgage under the merchant  
 22 shipping legislation.

23 Pennington, Company Law (8th Ed., 2001), Doc. 66-21, pg 13.

24 4. CAPITAL BANK did not register the subject mortgage as a "charge" with  
 25 Companies House, and as a consequence, its security is void as against a liquidator or  
 26 administrator:

27 Certain charges void if not registered.

28 (1) Subject to the provisions of this Chapter, a charge created by a

company registered in England and Wales and being a charge to which this section applies is, so far as any security on the company's property or undertaking is conferred by the charge, void against the liquidator or administrator and any creditor of the company, unless the prescribed particulars of the charge together with the instrument (if any) by which the charge is created or evidenced, are delivered to or received by the registrar of companies for registration in the manner required by this Chapter within 21 days after the date of the charge's creation.

(2) Subsection (1) is without prejudice to any contract or obligation for repayment of the money secured by the charge; and when a charge becomes void under this section, the money secured by it immediately becomes payable.

1985 Companies Act, Sec. 395.

5. If the Court rules against CAPITAL BANK's claims on the grounds that its mortgage did not satisfy the dual registration requirement under English law, *ipso facto*, if COVER DRIVE did comply with the dual registration is requirement, its mortgage must be given priority over CAPITAL BANK's.

6. Whether or not JUANITA or COVER DRIVE have standing to invoke the above-quoted provisions of Sec. 395, a liquidator clearly does. Assuming the imminent appointment of a liquidator for JUANITA in the United Kingdom, his or her avoidance of CAPITAL BANK's unregistered mortgage would relegate CAPITAL BANK to the status of a general unsecured creditor.

7. Insofar as foreign ship mortgages are concerned, the SMA permits only the enforcement of mortgages complying with foreign law, not those contravening it. How can a foreign mortgage "voided" in its country of origin still be granted preferred mortgage status under the SMA? Even where (unlike here) the correct recording procedures are followed, registration alone does not turn an invalid mortgage into a

1 valid preferred mortgage. *Bergren v. Davis*, 287 F.Supp. 52, 55 (D.Conn., 1968).

2 8. If, following avoidance by a liquidator, the subject mortgage can no longer  
 3 claim “preferred mortgage” status under the SMA, then subject matter jurisdiction no  
 4 longer exists. *Privilege Yachting, Inc. v. Teed*, 849 F.Supp. 298 (D.Del., 1994). In  
 5 deciding an earlier Motion to Dismiss, this Court ruled that Plaintiff’s registration at  
 6 ROSS was sufficient for purposes of subject matter jurisdiction even if (and without  
 7 deciding whether) CAPITAL BANK was obligated to comply with the dual registration  
 8 requirements of English Law. In the interests of judicial economy and preservation of  
 9 the record for appeal, BIRGITTA and/or COVER DRIVE will present evidence at trial  
 10 establishing that the dual registration (ROSS and Companies House) was mandatory  
 11 under English Law – an issue that was not reached by this Court in its earlier motion  
 12 ruling. A trial court decision on the mandatory dual registration issue will allow the  
 13 Court of Appeal to fully address BIRGITTA’s jurisdictional challenge, i.e., if the Court  
 14 of Appeals determines that ROSS registration alone was insufficient to establish the  
 15 existence of a preferred ship mortgage under the SMA if the BIRGITTA mortgage was  
 16 subject to the dual registration requirement, there would be no need to remand for a trial  
 17 court finding of whether the dual registration requirement applied to the BIRGITTA  
 18 mortgage. This Court will have already decided this latter issue, and the Court of  
 19 Appeal will be able to resolve the entire question based on the trial record.

20 **B. Key Evidence in Support of COVER DRIVE’s First Affirmative Defense**

21 1. Plaintiff admits (Stipulated Fact 34): “The BANK never registered The  
 22 Registrar of Seaman and Shipping (“ROSS”) Mortgage of a Ship (Exhibits 2 and 2A),  
 23 The Marine Loan (Exhibits 1 and IA), and the Marine Mortgage (Exhibits 3 and 3A) or  
 24 any summary of those documents or any document that referenced those documents  
 25 [with] the Registrar of Companies in the UK.” The additional key evidence in support  
 26 of this Affirmative Defense will be the testimony and documents referred to above  
 27 establishing that JUANITA had an established place of business in the UK and hence  
 28 the Plaintiff’s mortgage was subject to the dual registration requirements of English

1 law.

2 C. Elements of COVER DRIVE's Second Affirmative Defense

3 Second Affirmative Defense: Failure to Mitigate Damages

4 Claimant is informed and believes that Plaintiff has failed to  
5 mitigate its damages by, *inter alia*, failing in or about January 2007  
6 to accept a bona fide tender of payment in full for all of its claims  
7 in this litigation by Claimant.

8 1. Damages are a matter of substantive, rather than procedural, law. *In re Air*  
9 *Crash Disaster, etc.*, 982 F.2d 1271 (9 Cir., 1989).

10 2. The subject mortgage contains an English Law choice of law clause.

11 3. Under English Law, the plaintiff must take all reasonable steps to mitigate the  
12 loss which he has sustained and, if he fails to do so, he cannot claim damages for any  
13 such loss which he ought reasonably to have avoided. *British Westinghouse Electric*  
14 *and Manufacturing Co. Ltd. v. Underground Electric Rlys Co. of London Ltd.* [1912]  
15 AC 673 at 689.

16 4. Under English Law, the plaintiff must act not only in his own interests but  
17 also in the interests of the defendant and keep down the damages, so far as it is  
18 reasonable and proper, by acting reasonably in the matter. *Smailes & Son v. Hans*  
19 *Dessen & Co.* [1905] 94 LT 492 at 493.

20 D. Key Evidence in Support of COVER DRIVE's Second Affirmative Defense

21 1. Testimony and documents will establish: (a) it was commercially  
22 unreasonable and unnecessary to arrest the vessel in May 2006 because there had been  
23 no defaults and any payment, insurance, or navigation area issues could easily have  
24 been resolved without arresting the BIRGITTA; (b) Plaintiff unreasonably refused a  
25 good faith offer from a qualified third-party buyer made during January-March 2007 for  
26 an all cash payment of \$6.25 million which amount would have completely covered all  
27 of Plaintiff's damages and costs (interest, arrest costs, attorneys fees, and the  
28 outstanding balance of the loan.); and, (c) Plaintiff failed to reasonably monitor and



1 control the substitute custodians fees and costs.

2 E. Elements of COVER DRIVE's Third Affirmative Defense

3 Third Affirmative Defense: Existence of a Superior Security Interest

4 Under English law, Claimant has a fully perfected and duly  
 5 registered foreign ship mortgage on the BIRGITTA that is superior  
 6 to any interest that Plaintiff may have and Claimant's secured  
 7 interest substantially exceeds the current market value of the  
 8 BIRGITTA. Consequently, under English law Plaintiff, as an  
 9 unsecured creditor, is not entitled to recover any amount against  
 10 the BIRGITTA.

11 1. COVER DRIVE must establish that it has a duly registered ship mortgage on  
 12 the BIRGITTA in full conformity with the dual registration requirements of English  
 13 Law, and that CAPITAL BANK does not. According to Pennington, *supra*, Doc.  
 14 66-21, at pg. 14:

15 ...[A] ship mortgage registered first in the ship register but  
 16 unregistered in the company charges register loses the benefit of  
 17 first priority in the ship register through invalidation under the  
 18 companies legislation as against a subsequent mortgage registered  
 19 under both systems but registered only second in the ship register.  
 20 Ship registration cannot exclude the invalidation provision in the  
 21 company system. (emphasis added.)

22 F. Key Evidence in Support of COVER DRIVE's Third Affirmative Defense

23 1. CAPITAL BANK admits it did not register its mortgage with Companies  
 24 House. (Stipulated Fact 34.) In July 2007, the JUANITA Board of Directors formally  
 25 recognized JUANITA's \$10.5 million debt to COVER DRIVE for the unpaid purchase  
 26 price related to JUANITA's acquisition of the BIRGITTA in March 2005. JUANITA  
 27 granted COVER DRIVE a ship mortgage which COVER DRIVE timely registered with  
 28 both ROSS and Companies House in the UK. If liquidation proceedings for JUANITA



are underway by the time of trial, then proof of that fact will also be presented.

2. Documents and testimony establishing that COVER DRIVE registered its mortgage with both ROSS and with Companies House, including Joint Exhibit 290.

3. Documents and testimony establishing that JUANITA purchased the BIRGITTA from COVER DRIVE for conditional consideration, of which CAPITAL BANK knew or should have known prior to making the \$6 million loan to JUANITA, which consideration was rendered worthless through no fault of COVER DRIVE, as a consequence of which JUANITA granted a valid ship's mortgage to COVER DRIVE, which has priority over the CAPITAL BANK mortgage.

#### IV. Similar Statements for all Third Parties

There are no Third-Party Plaintiffs or Third-Party Defendants.

#### V. Anticipated Evidentiary Issues

The only currently anticipated evidentiary issues are those specified in Plaintiff's two pending Motions in Limine

#### VI. Issues of Law

COVER DRIVE anticipates the following issues of law:

1. Under English Law, whether JUANITA had an established place of business in the UK such that the Plaintiff's mortgage had to be registered at Companies House.

2. Under English Law, whether the COVER DRIVE 2007 ship mortgage, having been registered in full compliance with the dual registration requirements: (a) is a superior security interest; and (b) with or without a liquidation of JUANITA, is relegated Plaintiff to the status of a general unsecured creditor.

3. Under English law, whether JUANITA and/or BIRGITTA remained obligated to comply with certain mortgage obligations after the May 2006 arrest of the BIRGITTA if that arrest lacked legal and factual merit.

4. Under English Law, whether any mortgage obligations other than the obligation to repay the loan remained if the debt was automatically accelerated 21 days after its creation because the Plaintiff's mortgage was not registered at Companies

House.

5. Under English law, whether Cover Drive has a valid and enforceable mortgage on the BIRGITTA, which was duly registered with ROSS and Companies House and has priority over CAPITAL BANK's mortgage.

VII. Bifurcation of Issues

If a liquidation proceeding for JUANITA is initiated before trial begins, BIRGITTA contends it would be appropriate for the Court first to consider the subject matter jurisdictional issues created by the liquidation before proceeding with trial on the merits.

VIII. Jury Trial

Not applicable.

IX. Attorneys' Fees

Under English Law and the loan documents, attorneys fees may be awarded (Exhibit 1 paragraph 12.1).

X. Abandonment of Issues

COVER DRIVE has not abandoned any issues.

Dated: June 7, 2010

LAW OFFICES OF BRUCE IAN FAVISH

By: /s/ Bruce I. Favish  
Bruce I. Favish, Attorney for Specially  
Appearing Claimant COVER DRIVE INC.